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In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 924

HUDSON & MANHATTAN RAILROAD COMPANY,
PETITIONER

v.

WILLIAM J. HARDING, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION[1]

OPINIONS BELOW

The opinion of the Court of Appeals (Pet. App. 33–42) is reported at 229 F. 2d 616. The opinion of the District Court (Tr. App. 265–266)[2] has not been reported.

[1] The Commission became a party to the proceeding in the District Court pursuant to Section 208 of the Bankruptcy Act (11 U. S. C. 608) and appeared in the Court of Appeals urging affirmance of the orders involved (see Pet. App. 33).

[2] "Tr. App." refers to the appendix to the brief in the Court of Appeals of Herman T. Stichman, trustee of the debtor and an appellee in the court below. "App." refers to the appendix to the brief below of the appellant, petitioner here.

JURISDICTION

The judgment of the Court of Appeals (Pet. App. 43–44) was entered on February 9, 1956. The petition for a writ of certiorari was filed on May 4, 1956. The jurisdiction of this Court is invoked under Section 24 (c) of the Bankruptcy Act (11 U. S. C. 47 (c)).

QUESTIONS PRESENTED

1. Whether in a reorganization under Chapter X of the Bankruptcy Act the courts below correctly refused to authorize the hiring by the debtor of engineering experts to make a valuation of the debtor's properties for the purpose of disproving allegations relating to insolvency in the creditors' petition for reorganization, where the request for this action was made subsequent to court approval of the petition, and where this approval had been given in reliance upon the debtor's answer alleging that it could not meet its debts as they matured and joining in the prayer seeking reorganization under Chapter X.

2. Whether it was proper to deny petitioner's motion for leave to file, some three months after its original answer, an "answer de novo" seeking to relitigate jurisdictional issues which had already been resolved.

STATUTE INVOLVED

The pertinent sections of Chapter X of the Bankruptcy Act, 54 Stat. 709, as amended, 11 U. S. C. 401 *et seq.*, are set forth in Appendix C

to the petition for a writ of certiorari (Pet. App. 45–47).

STATEMENT

Petitioner (sometimes referred to herein as the debtor) is a corporation which owns and operates (1) an electric inter-urban railroad carrying passengers exclusively between New York City and nearby points in New Jersey through its tunnels under the Hudson River and (2) two large office buildings in New York City. It has funded debt due February 1, 1957, of approximately $57,000,000, including deferred interest (App. 10, 11, 12). It is alleged that in each of the years 1947 through 1953 the debtor lost from approximately $947,000 to $1,722,000 (Tr. App. 282).

The orders sought to be reviewed arose during the course of a proceeding under Chapter X of the Bankruptcy Act, which was instituted on August 11, 1954, by the filing of an involuntary petition in the United States District Court for the Southern District of New York by three bondholders of the debtor. The petition alleged *inter alia* that the debtor was a railroad corporation authorized by Chapter X to file a voluntary petition for reorganization thereunder, that it was unable to meet its debts as they matured, that it was insolvent, and that it had committed acts of bankruptcy by making preferential payments (Tr. App. 9–16).

On December 8, 1954, the debtor filed an answer consenting to the reorganization and joining in

so much of the petition as prayed for the reorganization. This followed the denial of a motion the debtor had filed to dismiss the petition on the ground that the debtor was operated as part of a general railroad system and hence not authorized to obtain relief under Chapter X and the simultaneous denial of an application by the debtor for approval of a voluntary petition it had filed on November 19, 1954, seeking reorganization under Section 77 of the Bankruptcy Act (11 U. S. C. 205). The consenting answer filed on December 8, 1954, like the Section 77 petition which the debtor had filed, expressly stated that the debtor was unable to meet its debts as they matured. This answer denied the allegations as to acts of bankruptcy, but, by failure to deny them, admitted the other allegations of the creditors' petition.[2] (Tr. App. 18–19.)

On December 14, 1954, the District Court approved the Chapter X petition upon "being satisfied that the petition, by reason of the debtor's answer, and consent to reorganization, complies with the requirements of Chapter X of the Bankruptcy Act and has been filed in good faith" (Tr. App. 20). No appeal was taken from this order.

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[2] In a preamble to the answer it was stated that the applicability of Chapter X was not conceded, but there was no express denial of the allegation that the debtor was a railroad corporation authorized by Chapter X to file a petition for reorganization thereunder.

On December 28, 1954, the debtor served a purported "amended answer" to the creditors' petition, which again specifically consented to the reorganization and joined in the prayer of the petition for reorganization. This answer was substantially in the same form as the original answer, but it denied various allegations of the petition (although not the allegation respecting the capacity of the debtor to file a Chapter X petition), and it specifically denied that the debtor was insolvent as well as that preferential payments had been made. No court approval of its filing was ever sought.

In the meantime, on December 22, 1954, a stockholder, pursuant to Section 137 of the Bankruptcy Act (11 U. S. C. 537), had filed an answer to the creditors' petition, which answer raised no question with respect to the jurisdiction under Chapter X, as distinguished from Section 77, but which denied among other things that the debtor was insolvent, that it had committeed any acts of bankruptcy, and that it was unable to meet its debts as they matured (Tr. App. 21–22).[4]

[4] Section 137 permits the filing of an answer controverting the allegations of a voluntary or involuntary petition, after its initial approval by the court under Section 141 or 142, by any creditor or indenture trustee, or if the debtor is not insolvent, by any stockholder of the debtor. On December 21, 1955, the District Court determined that the answer filed by the stockholder in this case should be treated as though it had been filed after a voluntary petition by the debtor, and, therefore, that the only material issue triable, assuming that the debtor was solvent, was whether or not the debtor was un-

Thereafter, when a pre-trial hearing had bee scheduled with respect to the stockholder's an swer, the debtor moved for authorization to re tain an engineering firm to appraise its property at the expense of the estate. In this connection the debtor urged that "the d ermination of the issue of insolvency by the Court is a condition t the reorganization of the Debtor and the adminis tration of its estate in this proceeding" (Tr. App 29), and it indicated that it expected to litigate at that time the question of its solvency (Tr. App 28, 50–52). The court denied the application on February 23, 1955 (Tr. App. 3), having stated: "I am going to hold now, as a matter of law, that insolvency or solvency is not an issue material to this proceeding so far as the debtor is concerned" (Tr. App. 52). The order to this effect (Tr. App. 3) is one of the two orders affirmed by the court below as to which the debtor seeks further review. The debtor then moved to withdraw its amended answer and to file an "answer de novo" (Tr. App. 36). The proposed "answer de novo," although not denying the allegation that the debtor could not meet its debts as they matured, omitted the specific affirmative allegation to that effect, and,

able to meet its debts as they matured. On this issue, the court received proof and found that "at the time the petition was filed the debtor was unable to meet its debts as they matured and that the previous approval of the petition for reorganization should be reaffirmed." *In re Hudson & Manhattan Railroad Company*, 138 F. Supp. 195, 203 (S. D. N. Y.).

unlike the earlier answer, did not consent to or join in the petition for reorganization (Tr. App. 43–44).

A hearing on this motion was held on March 3, continued on March 4, and adjourned over the weekend to March 7, 1955, on which day the debtor rested (Tr. App. 32, 253–254). At the hearing the debtor offered the testimony of Mr. Reid, president of the debtor and chairman of its board of directors, who had verified the answers. He testified that the purposes of the new answer sought to be filed were: to preserve for the junior security holders the right to assert that the debtor was solvent in order to participate in the reorganization, to preserve for the benefit of the directors the right to deny preferential acts, and to have the Chapter X proceeding dismissed because the debtor would be better off under Section 77 and the I. C. C. than under Chapter X and the S. E. C. (Tr. App. 170, 171, 212, 215–216, 221–222).[5]

The District Court denied the debtor's motion to withdraw its amended answer and file a new answer, finding that the proposal to file a new answer was without merit and not made in good faith. The order to that effect, entered April 7,

[5] It was not made clear how jurisdiction by the I. C. C. could be obtained in view of the fact that the debtor had not appealed from the order denying its motion to dismiss the Chapter X proceeding or from the order denying its application for approval of its Section 77 petition and the time to appeal from both orders had expired.

1955 (Tr. App. 4–8), is the second order affirmed by the court below as to which the debtor seeks further review in this Court. The court below found with respect thereto that there was "ample support" for the District Court's finding that the application "was not filed in good faith and that it was without merit." (Pet. App. 42.)

ARGUMENT

The orders sought to be reviewed, while appealable, are interlocutory and of a discretionary nature. We submit that the determinations of the courts below are correct and are not in conflict with holdings of other courts of appeals or of this Court. Although petitioner has attempted to phrase its first two questions presented in jurisdictional terms (Pet. 2–3), there is no serious problem of jurisdiction involved or any other problem of sufficient importance to warrant review by this Court. The third question which the petitioner asserts is involved (Pet. 3) is based on an interpretation by the court below of a procedural rule as to which the court correctly stated that a contrary determination "would not alter the result" (Pet. App. 39).

1. Despite the fact that petitioner joined in asking the relief sought by the creditors' petition and admitted allegations therein clearly sufficient to give the court jurisdiction over a debtor's petition, petitioner now urges that the District Court has no jurisdiction over this Chapter X proceed-

ing. The gist of petitioner's complaint is that allegations of the creditors' petition, which would have been essential had the debtor not joined in its request for relief, were not proved. Petitioner's position stems from the refusal of the District Court to permit petitioner to litigate an issue respecting its solvency after approval of the involuntary Chapter X petition.[6] The creditors' petition alleged that the debtor, while insolvent, had made a preferential transfer of its property. Such a transfer is an act of bankruptcy,[7] and a creditor's petition must allege the commission of an act of bankruptcy by the debtor within the preceding four months (in the absence of certain other allegations irrelevant here) in addition to the requirements applicable to a debtor's petition. Section 130 and 131 of the Act (11 U. S. C. 530 and 531). The only allegation respecting insolvency required in a debtor's petition, on the other hand, is that the debtor be "insolvent or unable to pay its debts as they mature." Section 130 (1) of the Act (11 U. S. C. 530 (1)). As we have noted, both petitioner's original and amended answer alleged that it was unable to meet its debts as they matured, and both joined in the prayer for reorganization.

[6] This was the basis of the District Court's denial of petitioner's application to have engineers employed at the expense of the estate for the purpose of determining petitioner's insolvency, the first order of which petitioner seeks further review.

[7] See Section 3 (a) (2) of the Act (11 U. S. C. 21 (a) (2)).